

**City of Lincoln  
Police and Fire Pension  
Statement of Investment Policy**

**I. Purpose**

The City of Lincoln Police and Fire Pension Plan (the Plan) is a defined benefit pension plan providing retirement, disability and survivor benefits to Police Officers, Fire Fighters and their beneficiaries. The system operates under the rules of Internal Revenue Code section 401(a). Plan benefits are paid by the City from the Police and Fire Pension Fund (the Fund). The Investment Board (the Board, as established by the City Council) has developed this Statement of Investment Policy to describe:

- A. The long-term investment objectives,
- B. The Responsibilities of the Board and Pension Administrators,
- C. The asset class allocation methodology,
- D. The investment selection criteria,
- E. The ongoing asset monitoring.

**II. Objectives**

The Investment Board's objective is to oversee the management of the assets of the Fund in a manner consistent with Lincoln Municipal Code and that expected from individuals of prudence, discretion, and intelligence in dealing with the property of another. Specifically:

- A. To have cash available for the Plan's benefit payments by structuring the Fund to provide income and/or liquidity to supplement tax revenues and employee contributions.
- B. To produce an asset class allocation, with a long term perspective, that will diversify the Fund over asset classes with distinctly different risk and return characteristics in weightings designed to minimize risk for any given level of desired return.
- C. To select appropriate investments, or investment managers, for each asset class.
- D. To timely monitor and adjust asset allocation and individual investments as needed.
- E. To provide Pension Administration the flexibility to manage the Fund within the guidelines detailed in this document.

**III. Responsibilities**

The Board shall have the responsibility for and direct all investments and reinvestments of the Fund and all sums credited to the Fund. The Board will meet at least semi-annually to formulate policies, strategies, determine the asset class allocation and select the managers for the investments within each asset class. The Board will also review transactions, cash flow needs and make changes as needed.

- A. The Plan Administration will implement the Board's investment decisions. Plan Administration will have the ability to buy and sell individual investments previously approved by the Board, within the framework of this policy, to provide cash for benefit payments and to re-balance the asset class allocation.

#### **IV. Asset Allocation Methodology**

With the help of a financial consultant, the Board will understand the risk and return characteristics of each asset class presented to it. The Board will weigh total return and cash flow objectives against the risk associated with various asset class combinations. For any given potential return target there are an infinite number of asset class combinations. The Board will hypothesize the future risk and return of each asset class given historical data, economic and financial projections, and assign appropriate allocation ranges and weightings to each asset class seeking to provide projected cash flows and minimize risk for the targeted level of return.

- A. The Fund is limited to the following asset classes. No other types of securities can be purchased. Permissible asset classes are as follows:
  - 1. Cash or Money Market: Short-term, high quality debt securities low in risk and highly marketable, such as commercial paper, certificates of deposit and repurchase agreements.
  - 2. Large Cap Value Equity: Funds in this asset class invest their equity assets primarily in companies with large market capitalizations. Large market capitalization is generally defined as being in excess of \$8 billion. Large cap value funds tend to focus on companies that are less expensive than the market as a whole. These firms may be out of favor with investors due to recent business problems or may simply be growing slower than other companies. These slow growers, which usually fall in the utilities, energy, financial and cyclical sectors, tend to pay relatively high dividends and have more stable stock prices. Funds in this asset class will normally have a below-average price-to-earnings ratio, price-to-book ratio and earnings growth ratio when compared to the diversified large cap funds average.
  - 3. Large Cap Growth Equity: Funds in this asset class invest their equity assets primarily in companies with market capitalizations. Large market capitalization is generally defined as being in excess of \$8 billion. Large cap growth funds tend to focus on companies that are projected to grow faster than the overall stock market. Many of these funds focus on rapidly expanding industries such as technology, health care and services. These funds will normally have an above-average price-to-earnings ratio, price-to-book ratio and earnings growth ratio when compared to the diversified large cap funds average.
  - 4. Mid Cap Value Equity: Funds in this asset class invest their equity assets in companies of all sizes, but generally focus on companies with market capitalizations of between \$2 and 8 billion. Mid cap value funds tend to emphasize companies that are considered undervalued compared to the market as a whole. These funds will normally have a below-average price-to-earnings ratio, price-to-book ratio and earnings growth ratio when compared to the diversified mid cap funds average.
  - 5. Mid Cap Growth Equity: Funds in this asset class invest their equity assets in companies of all sizes, but generally focus on companies with market capitalizations of between \$2 and 8 billion. Mid cap growth funds normally invest in companies with long-term earnings expected to grow significantly faster than the market and therefore command relatively higher prices. Many of

these funds emphasize rapidly expanding industries such as technology, health care and service. These funds will normally have an above-average price-to-earnings ratio, price-to-book ratio and earnings growth ratio when compared to the diversified mid cap funds average.

6. **Small Cap Value Equity:** Funds in this asset class invest their equity assets in companies with small market capitalizations. Small market capitalization is generally defined as being approximately \$2 billion or less. Small cap value funds seek long-term growth by investing in companies that are considered to be undervalued relative to the market. Many of these funds concentrate on undervalued stocks that have yet to be discovered by other investors, while others focus on stocks of troubled companies with management or growth problems. These funds will normally have a below-average price-to-earnings ratio, price-to-book ratio and earnings growth ratio when compared to the diversified small cap funds average.
7. **Small-Cap Growth Equity:** Funds in this asset class invest their equity assets in companies with small market capitalizations. Small market capitalization is generally defined as being approximately \$2 billion or less. Small cap growth funds normally invest in companies with long-term earnings expected to grow significantly faster than the overall stock market and tend to favor up-and-coming, rapid-growth industries. Because these businesses are in their early growth stages, these funds tend to be quite risky. These will normally have an above-average price-to-earnings ratio, price-to-book ratio and earnings growth ratio when compared to the diversified small cap funds average.
8. **International Equity:** International Equity funds invest in any country outside the U.S. Most of these funds divide their assets among a dozen or more developed markets including Japan, Britain, France and Germany. They tend to invest the rest in emerging markets such as Hong Kong, Brazil, Mexico and Thailand. Some funds are more aggressive in their country selection, which can cause them to carry additional risk.
9. **Corporate Bonds:** Debt instruments issued by corporations rather than governments. Corporate bonds are typically purchased with various maturity dates and qualities. Quality is measured by various rating agencies such as Moody's and Standard & Poors. Lower quality bonds will typically have higher yields, but will also have higher probability of default. Higher quality bonds will typically have lower yields, but less probability of default.
10. **Domestic Debt:** This asset class may contain Treasury, Agency or Corporate domestic investment grade debt. Block sizes shall have a minimum of \$100,000 and a maximum equal to the lesser of \$2,000,000 or 20% of the total asset class size.
11. **Convertible Securities:** A bond or preferred stock that can be converted into a predetermined amount of the company's equity at certain times during its life. Convertibles are sometimes called CVs. Convertible securities tend to offer a lower rate of return in exchange for the option to trade the security into common stock.
12. **Treasury Inflation Protected Securities:** A special type of Treasury note or bond that offers protection from inflation. As with other Treasuries, when you buy an inflation-indexed security you receive interest payments every six months and a payment of principal when the security matures. The difference is that the coupon payments and underlying principal are automatically increased to compensate for inflation by tracking the consumer price index (CPI). If U.S. Treasuries are the world's safest investments, then you might say that TIPS are the safest of the safe. This is because your real rate of return, which represents the growth of your

purchasing power, is guaranteed. The downside is that, because of this safety, TIPS offer a low return.

13. Foreign Bonds: Debt instruments issued by companies / governments domiciled outside of the United States. Foreign bonds typically carry a higher amount of risk due to currency fluctuations, political instability, and differing rating services.
14. Real Estate: Real Estate investments may invest domestically and take the form of a direct investment in a Private Investment Partnerships, a public or private REIT, or a Private Placement Agreement.
15. Alternative Investments: Alternative Asset investments may be invested in Funds of Hedge Funds. The objective of these investments shall be to reduce overall portfolio volatility, increase returns and prevent loss of principal.

- B. The Board will annually set minimum, maximum and target allocation percentages for each asset class described in section IV. A. Assets will be rebalanced at least once a year to the "Approved Target Allocation." The current percentages are listed below:

Asset Class	Min %	Max %	Target %
1. Cash, Stable Value or Money Market	0	10	1
2. Large Cap Value Equity	0	30	12.5
3. Large Cap Growth Equity	0	30	3
4. Mid Cap Value Equity	0	30	3
5. Mid Cap Growth Equity	0	30	3
6. Small Cap Value Equity	0	50	20
7. Small Cap Growth Equity	0	30	3
8. International Equity	0	20	5
9. Corporate Bonds	0	40	12
10. Domestic Bonds	0	40	7.5
11. Convertible Securities	0	20	2
12. Treasury Inflation Protected Securities	0	20	5
13. Foreign Bonds	0	20	5
14. Real Estate	0	30	15
15. Alternative Investments	0	20	3
Total			100

## **V. Investment Selection Criteria**

With the help of a financial consultant, the Board will employ sufficient qualitative and quantitative measures to prudently evaluate potential investment options once the asset class allocation is set and will award and retain those investment managers they believe have optimum future potential long term return and risk characteristics.

- A. Investment Disciplines: Investment managers should consistently invest in assets corresponding to their asset class and should demonstrate a reasonably consistent investment process.
- B. Performance Measures: Investment manager performance should be measured against appropriate benchmarks and peer groups based on investment objective, style and market capitalization. Investment performance should be competitive on a long-term basis within each appropriate asset class
- C. Access to investment information: Investment managers should be structured so as to provide easy access to return, risk and other relevant data.
- D. Manager Quality and Depth: Investment managers should have a history of reliability and a sound financial background. The manager should demonstrate quality and stability and apply a business approach that is consistent with the prudence investor rule.
- E. Fees: Investment managers expenses should be competitive when compared to similar offerings in the asset class peer group.

## **VI. Asset Allocation and Investment Monitoring**

With the help of a financial consultant, the Board will annually review asset class allocation in accordance with the Asset Allocation Methodology described in policy section IV and the Board will review individual investments in accordance with the Investment Selection Criteria described in policy section V. Additionally, the Board will review individual investments for their adherence to the following:

- A. Investment Discipline: Each Investment Manager will be monitored for adherence to stated investment disciplines and asset class style drift. If it is judged that an investment is subject to significant style drift, the investment will be put on a watchlist.
- B. Investment Management: Investment management should remain consistent. A change in one or more key managers will require the investment be put on watchlist and the investment characteristics and performance will be monitored to assure they do not significantly change under the new management.
- C. Performance Standards. Funds are expected to meet or exceed their benchmark identified by the fund's asset consultant. In the event a fund fails to meet its performance standards in three of the past four quarters, the fund will be placed on a watchlist. If no comparable benchmark or investment exists the fund will be monitored to assure it is meeting its intended objective.

Any fund that is on watchlist will be reviewed at each semi-annual Board meeting to determine why it is not meeting the stated benchmarks and if further action is warranted. A fund can be removed from watchlist for one of three reasons:

- The fund performance changes so that it meets or exceeds its investment benchmarks.
- The Board understands why the fund is not meeting a stated benchmark and is comfortable that the fund is still meeting the objective for which it was chosen.
- The Board replaced the fund.